GAO's Mission

The Government Accountability Office, the audit, evaluation and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday, GAO posts newly released reports, testimony, and correspondence on its Web site. To have GAO e-mail you a list of newly posted products every afternoon, go to www.gao.gov and select "Subscribe to Updates."

Order by Mail or Phone

The first copy of each printed report is free. Additional copies are $2 each. A check or money order should be made out to the Superintendent of Documents. GAO also accepts VISA and Mastercard. Orders for 100 or more copies mailed to a single address are discounted 25 percent. Orders should be sent to:

U.S. Government Accountability Office
441 G Street NW, Room LM
Washington, D.C. 20548

To order by Phone: Voice: (202) 512-6000
TDD: (202) 512-2537
Fax: (202) 512-6061

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

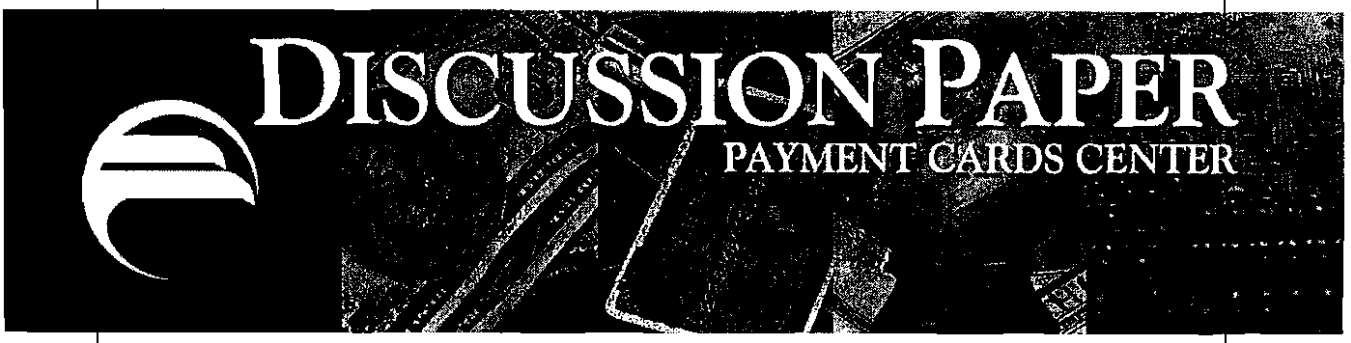
Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Gloria Jarmon, Managing Director, JarmonG@gao.gov (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, D.C. 20548

Public Affairs

Paul Anderson, Managing Director, AndersonP1@gao.gov (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, D.C. 20548



The Debate Over the National Bank Act and the Preemption of State Efforts to Regulate Credit Cards*

Mark Furletti**

March 2004

Summary: *The National Bank Act (NBA), the 140- year-old statute that led to the creation of nationally chartered banks, has likely been one of the most influential forces in the formation and development of the U S credit card industry The NBA gives nationally chartered banks a wide range of powers and protections One of these protections, the ability to disregard certain state laws, is currently at the center of a very heated debate. The regulator of national banks, the OCC, recently issued a rule that interprets the act as essentially preempting most state efforts to protect credit card consumers. State attorneys general, consumer advocates, and members of Congress have charged that the OCC's ruling is overly aggressive and results in bad public policy. This paper examines the current debate over preemption and its regulatory consequences. It analyzes how the expanding scope of preemption has affected the development of the credit card industry and the likely impact of the current debate on the industry's future*

** Payment Cards Center, The Federal Reserve Bank of Philadelphia, Ten Independence Mall, Philadelphia, PA 19106. E-mail: mark.furletti@phil.frb.org. Thanks to Rick Lang, Peter Burns, Bob Hunt, Melissa Jacoby, Elizabeth Schiltz, and Justin Kaufman. The views expressed here are not necessarily those of this Reserve Bank or of the Federal Reserve System.

I. Introduction

Nationally chartered banks underwrite almost three-quarters of the credit card loans made in this country.[1] Over the past two decades, these banks have relied on the National Bank Act ("NBA")[2] to preempt a variety of state and municipal regulations involving credit card interest rates, fees, and disclosures.[3] Recent state and municipal efforts to require national banks to adhere to local predatory lending laws, although directed at home equity and mortgage lending rather than credit card lending, have significantly raised the profile of the preemption debate.[4] The Office of the Comptroller of the Currency ("OCC") (the regulator of national banks) and various state authorities are engaged in a battle over the NBA's preemption power. This battle involves principles of federalism that are almost 200 years old[5] and is of intense interest to state attorneys general, consumer groups, industry executives, and bank regulators.[6] The courts, through the interpretation of the NBA, have repeatedly ruled against the states and municipalities when they have attempted to enforce their own consumer protection laws against out-of-state nationally

---

[1] As of Deeember 31, 2002, national banks held almost $400 billion of the $550 billion in U.S. managed bank card loans. Call Report Data. National Information Center (data on file with author). For additional statistics on national hank credit card lending, *see* Mark Furletti, *Measuring Credit Card Industry Chargeoffs A Review of Sources and Methods*, Federal Reserve Bank of Philadelphia Discussion Paper, at 23 (Oct. 2003) (*available at* http://www.phil.frb.org/pcc/discussion/measuring_chargeoffs.pdf).
Under our country's dual banking system, banks have the option of seeking either a state or national charter. A national bank has a charter approved by the Office of the Comptroller of the Currency and is primarily regulated by that agency. A state bank has a charter approved by the regulatory authority of the state in which it is located and can be primarily regulated by that authority as well as the Federal Reserve, or by that authority and the FDIC. Board of Governors of the Federal Reserve System, THE FEDERAL RESERVE SYSTEM: PURPOSES AND FUNCTIONS 1-7, 71-73 (1994).

[2] Act of June 3, 1864, c. 106, 13 Stat. 99, as amended (codified at 12 U.S.C. §§ 1, 2, 3, 4, 8, 11, 12, 13, 14, 21, 22, 23, 24, 26, 27, 29, 35, 39, 52, 53, 56, 57, 59, 60, 61, 62, 66, 71, 72, 73, 74, 75, 76, 81, 84, 85, 86, 90, 91, 93, 94, 141, 142, 143, 144, 161, 165, 181, 182, 192, 193, 194, 196, 481, 482, 483, 484, 485, 541, 548; 19 U.S.C. § 197; 31 U.S.C. § 543.38).

[3] *See, e g*, Marquette Nat'l Bank of Minn. v. First Omaha Serv. Corp., 439 U.S. 299 (1978) (finding NBA preempts state credit card interest rate ceiling); Greenwood Trust Co. v. Commonwealth of Mass., 971 F.2d 818 (1st Cir. 1992) (finding NBA preempts state credit card late fee restriction); Am. Bankers Assoc. v. Lockyer, 239 F. Supp. 2d 1000 (E.D. Cal. 2002) (finding NBA preempts state credit card disclosure law).

[4] *States Strike Back*, AMERICAN BANKER, Aug. 28, 2003, at 9.

[5] *See, e g*, McCulloch v. Maryland, 17 U.S. 316 (1819) (holding state tax on Bank of the United States unconstitutional because states lacked power to burden operations of nation's central bank).

[6] Comptroller of the Currency John D. Hawke, Jr., Remarks to Women in Housing and Finance (Sept. 9, 2003) (transcript available at http://www.occ.treas.gov/).

chartered banks.[7] These rulings, coupled with the OCC's vigorous assertion of preemption, have not stifled state efforts to regulate.[8] Some observers, however, have characterized this most recent fight over state predatory lending laws as "the states' Alamo."[9]

This paper will examine the regulatory consequences of the NBA's near total preemption of state statutes designed to protect credit card consumers.[10] Part II of this paper describes the interpretation of the NBA as it relates to the credit card industry and proposes an analytical framework for thinking about consumer-protection-type preemption. This section also analyzes the legal basis for the NBA's expanding scope of state law preemption, including relevant case law and regulatory pronouncements. Part III provides an overview of how expanded NBA preemption has affected the development of the credit card industry and consumers' access to credit. Part IV examines the current debate over preemption and its regulatory consequences for the credit card industry.

The paper concludes that the current debate over preemption will likely have little regulatory effect on the card industry in the near term. Recent interpretations of the NBA make the legal environment at the state level for card issuers much more predictable. States, in effect, have no authority to provide their resident cardholders with consumer protections, as this power is exclusively reserved to the federal government under the OCC's ruling. To the extent history can be a guide, any future regulation of credit cards by Congress is likely to be targeted and in response to demands for specific consumer protections.

---

[7] *Id. See also infra* note 57 (listing cases in which states have failed at attempts to enforce state laws against nationally chartered banks).

[8] *See, e.g.*, CAL. CIV. CODE § 1748.13 (2003) (imposing disclosure requirements on card issuers who have customers in California).

[9] *States Strike Back, supra* note 4, at 9.

[10] This paper will not consider the broader issues of federalism raised by the preemption of state laws. For a discussion of such issues, see THE FEDERALIST NOS. 44, 45, 46 (James Madison).

II. The Scope of NBA Preemption With Regard to Credit Card Industry Regulation

A. The National Bank Act's Power of Preemption

The National Banking Act of 1863 and the National Bank Act of 1864 ("NBA") established a federally chartered banking system.[11] In 1863, just prior to the passage of the NBA, all 1466 of the country's banks were state-chartered institutions.[12] Congress created the new system to provide for a national and uniform currency and to help stabilize the economy during and after the Civil War.[13]

To oversee the new national system, Congress created a federal agency within the Department of the Treasury called the Office of the Comptroller of the Currency ("OCC").[14] The NBA gives the OCC the power to examine, supervise, and regulate all national banks and to protect national banks from what the OCC describes as "potentially hostile state interference."[15] States, however, are not powerless in relation to nationally chartered banks. Although the NBA establishes a federal banking system independent of state control, in certain instances, it calls for the application of the laws of the state in which a national bank is chartered.[16] For example, even today, a national bank must adhere to the interest rate ceiling established by the legislature of the state in which it is organized (i.e., its home state).[17] National banks may also have to adhere to non-home-state contract, debt collection, taxation, zoning, criminal, and tort laws.[18]

---

[11] RAYMOND NATTER, FORMATION AND POWERS OF NATIONAL BANKING ASSOCIATIONS 2.3-2.4 (1983).
[12] *Id.* at 1.2-1.3.
[13] *See* Bank Activities and Operations; Real Estate Lending and Appraisals, 68 Fed. Reg. 46,119, 46,120 (proposed August 5, 2003) [hereinafter "*Bank Activities*"] (to be codified at 12 C.F.R. pt. 7,34) (describing legislative history of National Bank Act).
[14] *Id*
[15] *Id.*
[16] *Id* at 46,129.
[17] *See* First Nat'l Bank of Omaha v. Marquette Nat'l Bank of Minn., 636 F.2d 195 (8th Cir. 1980) (holding that national banks must adhere to their home state usury laws).
[18] *See, e.g.*, Bank of Am. v. City and County of San Francisco, 309 F.3d 551, 559 (9th Cir. 2002) (describing state powers to regulate national banks); *Bank Activities*, *supra* note 13 at 46,131 (explaining that these laws apply to extent to which they "incidentally affect" lending activities).

The majority of disputes involving nationally chartered credit card banks[19] and the NBA concern whether the laws of a state *that is not the bank's home state* can be applied to the card-issuing bank.[20] The extent to which these laws are overridden or "preempted" by the NBA is the key legal issue in most of these cases.[21]

The broad authority granted to the OCC by the NBA, along with the operation of the Supremacy Clause of the United States Constitution,[22] is the basis of the OCC's power to preempt state banking laws.[23] Preemption occurs when the laws of a particular government (e.g., the federal government) supercede those of another government (e.g., a state or municipal government).[24] There are essentially three theories of preemption on which the Supreme Court has relied: "express" preemption, "field" preemption, and "conflict" preemption.[25] The first involves Congress directly stating in the language of an act that it is preempting state law (e.g., this federal law supercedes state law).[26] The second theory of preemption, commonly referred to as "field" preemption, occurs when, regardless of whether it explicitly or implicitly preempts

---

[19] Nationally chartered credit card banks are national banks that issue general purpose credit cards (i.e., Visa, MasterCard, American Express, or Discover credit cards).

[20] *See, e.g.,* Marquette Nat'l Bank of Minn. v. First Omaha Serv. Corp. 439 U.S. 299 (1978) (addressing whether Minnesota usury statute applied to nationally chartered bank organized in Nebraska); Tikkanen v. Citibank (S.D.) N.A., 801 F. Supp. 270 (D. Minn. 1992) (addressing whether Minnesota usury statute applied to nationally chartered banks located outside of Minnesota); Ament v. PNC Nat'l Bank, 849 F. Supp. 1015 (W.D. Pa. 1994) (addressing whether Pennsylvania usury statute applied to nationally chartered banks located outside of Pennsylvania).

[21] *Id*

[22] U.S. CONST. art. VI, cl. 2. The clause reads as follows:

> This Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, anything in the Constitution or laws of any State to the contrary notwithstanding.

[23] *Bank Activities, supra* note 13, at 46,120.

[24] *See generally* Richard H. Fallon, Jr. et al., HART & WECHSLER'S THE FEDERAL COURTS AND THE FEDERAL SYSTEM 723-730 (describing principles of federal preemption of state law). *See also* Rice v. Santa Fe Elevator Corp., 331 U.S. 218 (1947) (defining principles of preemption).

[25] Michigan Canners and Freezers Ass'n, Inc. v. Agricultural Marketing and Bargaining Bd., 467 U.S. 461, 469 (1984).

[26] *See, e.g.*, Federal Boat Safety Act, 46 U.S.C § 4306 (1983) (expressly preempting state efforts to regulate recreational watercraft).

state law, Congress indicates that it intends federal law to "occupy an entire field of regulation."[27] "Field" preemption requires states to abandon any regulatory activity in that field.[28] Finally, federal law can trump a state law under the theory of "conflict preemption."[29] Even if Congress has not preempted an entire field, it can preempt any state law that is in direct conflict with federal law[30] or any state law that "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[31]

The ways by which the NBA preempts state consumer protection laws are complex and not easily categorized. This paper proposes that there are essentially two distinct strands of preemption: one involving section 85 of the act[32] and another involving section 24(Seventh).[33] The lines that divide these two strands, however, are not always as clear as the framework may suggest.[34] The extent to which these lines are blurred is discussed later in this section. Thinking about the strands as distinct and discrete, however, makes it easier to understand NBA preemption and analyze its consequences.

---

[27] *See, e g* , Conference of Fed. Sav and Loan Ass'ns v. Stein, 604 F.2d 1256 (9th Cir. 1979) (holding that regulatory control of the Federal Home Loan Bank Board over federal savings and loan associations is so pervasive as to leave no room for state regulatory control).

[28] *Michigan Canners and Freezers Ass'n, Inc* , 467 U.S. at 469.

[29] *See* Freightliner Corp. v. Myrick, 514 U.S. 280, 287 (1995) (evaluating whether National Traffic and Motor Vehicle Safety Act and state common-law were in conflict).

[30] *See, e g* , Gade v. Nat'l Solid Wastes Mgmt. Ass'n, 505 U.S. 88 (1992) (finding that state regulation of occupational safety and health issues was preempted because it was in conflict with Occupational Safety and Health Act)

[31] Michigan Canners and Freezers Ass'n, Inc , 467 U.S. at 469 (quoting Hines v. Davidowitz, 312 U.S. 52, 67 (1941)).

[32] 12 U.S.C. § 85 (2004). The NBA addresses interest rate regulation as follows:

> Any association may take, receive, reserve, and charge on any loan or discount made, or upon any notes, bills of exchange, or other evidences of debt, interest at the rate allowed by the laws of the State, Territory, or District where the bank is located, or at a rate of 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater, and no more, except that where by the laws of any State a different rate is limited for banks organized under state laws, the rate so limited shall be allowed for associations organized or existing in any such State under title 62 of the Revised Statutes.

[33] 12 U.S.C. § 24(Seventh) reads as follows:

> [A national banking] association shall . . . have power . . . [t]o exercise . . . all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; . . . by loaning money on personal security...

[34] See *infra* Part II.D discussing complexities of two preemption strands.

The first strand of preemption, based on section 85, involves non-home-state regulation of credit card pricing (such as interest rates, fees, or other price-related items).[35] Typically, substantive state laws are preempted by substantive federal laws. For example, the Fair Credit Reporting Act[36] explicitly preempts state laws that provide consumers with certain protections concerning the privacy of their credit data.[37] In lieu of these state protections, the FCRA gives consumers a host of federal protections.[38] Similarly, federal laws that address environmental problems, such as the Clean Air Act and Clean Water Act, preempt existing state statutes and set forth federal environmental standards.[39] Section 85 of the NBA, the section that preempts price-related state regulation, is different. It preempts state lending laws not to make way for federal laws about credit card pricing, but to make way for the laws of states in which card issuers are headquartered.[40] In this way it preempts non-home-state lending statutes with home-state lending statutes.

Recently, the NBA has been read to preempt state laws in a second way. Section 24(Seventh) has been interpreted as preempting all state laws involving *non-price-related* consumer protection regulation (e.g., disclosure requirements).[41] This second strand of preemption is also unique. It preempts not to make way for a comprehensive federal consumer protection scheme, but to make way, to a large extent, for a loose patchwork of federal regulation.

Overall, the OCC has used the preemption powers read into the NBA to stop various state and municipal efforts to regulate card issuers over the past 25 years.[42] The next two subsections will detail how sections 85 and 24(Seventh) have been interpreted as preempting a host of price-

---

[35] See *infra* Part II.B for a detailed discussion of section 85.
[36] Fair Credit Reporting Act §§ 601-24, 15 U.S.C. §§ 1681-1681(u) (2002).
[37] 15 U.S.C. § 1681t(2) (2002).
[38] 15 U.S.C. § 1681a (2002).
[39] *See* Clean Water Act, 42 U.S.C. §§ 1251-1387 (2000) (preempting state drinking water regulations); Clean Air Act, 42 U.S.C. §§ 7401-7671q (2000) (preempting state emissions regulations)
[40] *See, e.g.*, Marquette Nat'l Bank of Minn. v. First Omaha Serv. Corp. 439 U.S. 299 (1978) (interpreting the NBA as allowing national banks to export home-state interest rates).
[41] See *infra* Part II.C discussing section 24(Seventh) preemption.
[42] See *infra* Parts II.B and II.C discussing how OCC has used NBA to preempt state regulatory efforts.

and non-price-related consumer protection laws enacted by states to protect credit card consumers.

B. Preemption Under Section 85 of the NBA

Before the Supreme Court interpreted the NBA as preempting non-home-state credit card interest rate laws, card issuer regulation varied by state. Many states imposed ceilings on the interest rates that credit card issuers could charge consumers.[43] Regardless of where a national bank was chartered or located, it typically followed the specific usury laws of the states in which it marketed credit cards.[44] For example, a Maryland-based, nationally chartered card issuer followed Ohio usury laws when offering credit cards to consumers in Ohio and Pennsylvania usury laws when offering credit cards to consumers in Pennsylvania. Effectively, nationally chartered banks with customers throughout the entire country could have had 51 different regulators of interest rates on credit card loans (i.e., 50 state regulators and the OCC).[45]

The Supreme Court's 1978 decision in *Marquette National Bank of Minneapolis v. First Omaha Service Corporation*[46] clarified the role of state usury laws.[47] In *Marquette*, a national bank chartered in Minnesota (Marquette) sued a competing national bank chartered in Nebraska (First Omaha) for violating a Minnesota usury statute.[48] The Court decided that First Omaha did

---

[43] DAVID EVANS & RICHARD SCHMALENSEE, PAYING WITH PLASTIC, 71-72 (MIT Press 2000).

[44] *Id* at 82. *See also* Robert Johnston, *Nation-Spanning Credit Cards*, MONTHLY REVIEW (Federal Reserve Bank of San Francisco) (March 1972) (describing how state interest rate regulation hurt card bank profits). For a discussion of the history of state usury laws and the ways in which they restricted lending practices, see LENDOL CALDER, FINANCING THE AMERICAN DREAM (1999).

[45] *See, e g*, Diane Ellis, *The Effect of Consumer Interest Rate Deregulation on Credit Card Volumes, Charge-Offs, and the Personal Bankruptcy Rate*, FDIC Bank Trends No. 98-05, March 1998 (*available at* http://www.fdic.gov/bank/analytical/bank/bt_9805.html) (explaining effect of *Marquette* on banking deregulation).

[46] 439 U.S. 299 (1978).

[47] Although *Marquette* is credited with changing interest rate exportation practices (i.e., the ability of a bank to charge its home-state interest rate to an out-of-state resident), some courts prior to 1978 held that national banks could choose to charge a credit card customer the higher of the bank's or customer's home state usury ceiling rate. *See, e.g*, Fisher v. First Nat'l Bank of Omaha, 548 F.2d 255 (8th Cir. 1977) (holding that a national credit card bank located in Nebraska could charge a customer living in Iowa highest rate allowed by either state); Fisher v. First Nat'l Bank of Chicago 538 F.2d 1284 (7th Cir. 1976) (holding that a credit card bank located in Illinois could charge a customer living in Iowa highest rate allowed by either state).

[48] 439 U.S. at 301.

not have to comply with the Minnesota statute,[49] clearing the way for nationally chartered credit card issuers to export credit card rates from their own state to any other state in the country.[50] The Supreme Court's decision was based on section 85 of the NBA.[51] Section 85 allows national banks to charge an interest rate as high as that allowed by the usury laws of the state where the bank is "located."[52] Marquette asserted that First Omaha was "located" in Minnesota, where its credit cards were used to effect transactions.[53] The Court found, however, that the location of a national bank can only be the one state that is listed on the bank's certificate of organization – essentially the state where the bank is headquartered.[54] To interpret section 85 any other way, the Court reasoned, would render the term "location" meaningless and lead to the destruction of the nation's complex system of interstate bank lending.[55] Overall, the *Marquette* ruling found that the NBA effectively preempted the interest rate regulations of the 49 states in which a card issuer could not actually be organized.[56]

For over a decade after *Marquette*, nationally chartered card issuers faced little section 85 litigation. In the early 1990s, however, consumers challenged a variety of credit card fees as violating the usury statutes of the states in which they lived.[57] Cardholders asserted that the late,

---

[49] *Id*

[50] It is interesting that First National Bank of Omaha (First Omaha) ultimately sued Marquette National Bank for lobbying the Minnesota legislature to pass the interest rate ceiling statute at issue in *Marquette*. Agreeing with the Minnesota District Court's assessment that Marquette's lobbying did not violate federal law, the Eighth Circuit Court of Appeals dismissed First Omaha's claim. First Nat'l Bank of Omaha v. Marquette Nat'l Bank of Minn., 636 F.2d 195 (8th Cir. 1980).

[51] 12 U.S.C. § 85 (2004).

[52] *Id*

[53] *Marquette*, 439 U.S. at 310-11.

[54] *Id* at 310.

[55] *Id*. at 312.

[56] Despite *Marquette*, nationally chartered credit card issuers continue to defend themselves against claims that non-home-state interest ceilings apply. *See, e g* . Patten v. Maryland Bank, N.A., 2003 WL 21309046 (Tex. Ct. App. 1st Dist. 2003) (striking down claim that nationally chartered bank located in Delaware is bound by Texas interest rate ceiling). For a criticism of *Marquette's* legal reasoning and public policy implications, *see* Ralph J. Rohner. *Marquette Bad Law and Worse Policy*, 1 J. RETAIL BANKING 76 (1979).

[57] *See* Nelson v. Citibank (S.D.) N.A., 794 F. Supp. 312 (D. Minn. 1992) (arguing that late and over limit fees violated state statute); Tikkanen v. Citibank (S.D.) N.A., 801 F. Supp. 270 (D. Minn. 1992) (arguing that late and over limit fees violated state statute); Mazaika v. Bank One, Columbus, N.A., 1992 WL 1071450 (Pa. Ct. Com. Pl. 1992) (arguing that annual, late, return check, and over limit fees violated state statute); Ament v. PNC Nat'l Bank, 849 F. Supp. 1015 (W.D. Pa. 1994) (arguing that annual, late, return check, and over limit fees violated state statute); Copeland v. MBNA Am. Bank, 907 P.2d 87 (Co. 1995)

over limit, return check, and annual fees that their out-of-state card issuers charged were prohibited by the cardholders' home state usury laws.[58] In response, national banks asserted that these usury statutes were preempted by the NBA. With only one exception,[59] courts sided with the banks.[60]

Section 85 permits a national bank to charge "interest at the rate allowed by the laws of the State" in which the bank is organized.[61] Although *Marquette* cleared the way for the exportation of the highest interest rate allowed by the laws of an issuer's home state, it did not specifically address whether home-state-allowed fees (e.g., late, over limit, return check fees) could be exported. The Third Circuit U.S. Court of Appeals,[62] the U.S. District Court for the District of Minnesota,[63] and the Supreme Courts of Colorado,[64] Pennsylvania,[65] and New Jersey,[66] among others, have ruled on this issue.

(arguing that late fees violated state statute); Spellman v. Meridian Bank (Del.) 1995 WL 764548 (3d Cir. 1996) (arguing late fees violate state usury statute). In 1995, it was estimated that there were at least 32 late fee cases pending in state and federal courts. Denise Gray, *A Penalizing Ruling on Penalty Fees*, CREDIT CARD MANAGEMENT, Mar. 1, 1995, at 18.

[58] *See* Tikkanen v. Citibank (S.D.) N.A., 801 F. Supp. 270 (D. Minn. 1992) (arguing that late and over limit fees charged by out-of-state federally chartered bank violated state statute)

[59] *See* Sherman v. Citibank (S.D.) N.A., 668 A.2d 1036 (N.J. 1995) (ruling that late fees violated New Jersey usury statute).

[60] While this paper focuses on the NBA and nationally chartered, OCC-supervised credit card banks, courts also preempted state usury laws as they applied to state-chartered, FDIC-insured credit card banks (see *supra* note 1 for a description of state-chartered banks). Relying on a provision in the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) (12 U.S.C. § 3501 (1982)) that is similar to section 85 of the NBA, courts struck down various state usury law challenges. *See, e.g.*, Greenwood Trust Co. v. Mass., 971 F.2d 818 (1st Cir. 1992) (holding that state statute prohibiting imposition of late fee by state-chartered, federally insured bank was preempted by DIDMCA); Hill v. Chem. Bank, 799 F. Supp. 948 (D. Minn. 1992) (holding that state statute prohibiting imposition of late and over limit fees by state-chartered, federally insured bank was preempted by DIDMCA); *but see* Hunter v. Greenwood Trust Co., 668 A.2d 1067 (N.J. 1995) (holding that state statute prohibiting imposition of fees is not preempted by DIDMCA as to state-chartered, federally insured credit card bank). For a description of the DIDMCA and an analysis of the preemption issues it raises, see Elizabeth Schiltz, *The Amazing, Elastic, Ever-Expanding Exportation Doctrine and Its Effect on Predatory Lending Regulation*, 88 MINN. L. REV. 518, 565-69 (2004).

[61] 12 U.S.C. § 85 (2004).

[62] *See* Spellman v. Meridian Bank (Del.) 1995 WL 764548 (3d Cir. 1996) (holding that state statute limiting late and over limit fees charged by out-of-state federally chartered bank was preempted by NBA).

[63] *See* Tikkanen v. Citibank (S.D.) N.A., 801 F. Supp. 270 (D. Minn. 1992) (holding that state statute limiting late and over limit fees charged by out-of-state federally chartered bank was preempted by NBA); Nelson v. Citibank (S.D.) N.A., 794 F. Supp. 312 (D. Minn. 1992) (same).

The decision in *Spellman v. Meridian Bank (Delaware)*[67] is generally representative of the reasoning and analysis that many of these courts used to evaluate the meaning of the word "interest" and answer the fee exportation question. *Spellman* involved 11 consolidated actions brought in Pennsylvania courts against nationally chartered banks.[68] One of the questions presented to the three-judge panel was whether the word "interest" as used in section 85 of the NBA included fees.[69] The Third Circuit began its analysis by examining the plain meaning of the statute's language. It found that the word "interest," as used in section 85, was ambiguous.[70] The Court then looked to the NBA's 100-year-old legislative history and its subsequent interpretation by the courts. Although the legislative materials from 1864 (the time of the bill's passage) were not particularly instructive, the panel found that an interpretation of the NBA by the Supreme Court just 10 years after the act's passage was insightful.[71] In *Tiffany v. Nat'l Bank of Missouri*,[72] the Supreme Court addressed the issue of whether a national bank in Missouri was limited by the interest rate ceiling imposed on state banks by Missouri or whether it could charge a higher rate made available to other non-Missouri lenders in the state.[73] In finding that national banks could charge the highest rate allowed to any lender in the state, the *Tiffany* court interpreted the NBA as establishing national banks as "national favorites" that should be free from banking regulations

---

[64] *See* Copeland v. MBNA Am. Bank, 907 P.2d 87 (Co. 1995) (holding that state statute limiting late and over limit fees charged by out-of-state federally chartered bank was preempted by NBA); Richardson v. Citibank (S.D.) N.A., 908 P.2d 532 (Co. 1995) (same).

[65] *See* Bank One, Columbus, N.A. v. Mazaika, 680 A.2d 845 (Pa. 1996) (holding that state statute limiting penalty fees charged by out-of-state federally chartered bank was preempted by NBA).

[66] *See* Sherman v. Citibank (S.D.) N.A., 668 A.2d 1036 (N.J. 1995) (ruling that late fees violated New Jersey usury statute).

[67] *Spellman*, 1995 WL 764548.

[68] *Id* at *1.

[69] *Id.*

[70] *See id.* at *14 (explaining why it found the term ambiguous).

[71] *Spellman*, 1995 WL 764548 at *15.

[72] 85 U.S. 409 (1874).

[73] *Id* at 410-11. Although state legislatures often capped the interest rate that state banks could charge consumers, during the 1980s they allowed other lenders, such as those that financed automobiles and durable consumer goods, to charge higher rates. Essentially, nationally chartered card issuers wanted to be able to charge the higher of the state bank or consumer lender rates. Glenn B. Canner & Charles A. Luckett, *Developments in the Pricing of Credit Card Services*, FEDERAL RESERVE BULLETIN 652 (Sept. 1992).

that could hinder their lending efforts.[74] It also asserted that Congress' ultimate goal in passing the NBA was to help national banks actually take the place of state banks.[75]

The Third Circuit relied on the "most favored lender" doctrine articulated in *Tiffany* and the interest rate exportation ruling in *Marquette* as persuasive evidence that Congress intended national bank lending activities to be especially protected from state intervention.[76] In light of this intent, the *Spellman* court examined whether "interest" should be interpreted narrowly (i.e., not to cover fees), so as to allow all 50 states to regulate a critical pricing component of credit card loans made to their residents, or broadly, so as to allow national banks to be free from non-home-state fee regulation.[77] It concluded that restricting interest to non-fee finance charges would result in "an unworkable and undesirable hodgepodge" of state regulation that would favor certain state lenders over national bank lenders.[78]

In support of its decision, the Third Circuit cited other courts that had interpreted the word "interest" broadly so as to include commissions, closing costs, and penalty fees.[79] It also relied on the OCC's interpretation that "interest" includes all fees that offset the costs of risky cardholder behavior (e.g., paying late, charging over your credit limit) or the costs of opening and maintaining an account.[80]

---

[74] *Id.* at 412-13.

[75] The Court asserted:

> National banks have been National favorites. They were established for the purpose, in part, of providing a currency for the whole country, and in part to create a market for the loans of the General government. It could not have been intended, therefore, to expose them to the hazard of unfriendly legislation by the States, or to ruinous competition with State banks. On the contrary, much has been done to insure their taking the place of State banks.

Id. at 413.

[76] *Spellman*, 1995 WL 764548 at *16.

[77] *Id.*

[78] *Id.*

[79] *Id.* at *17 (citing, inter alia, Citizens' Nat'l Bank v. Donnell, 195 U.S. 369, 373-74 (1904) (penalty charges for late payment included). *See also* Greenwood Trust Co. v. Commonwealth of Mass., 971 F.2d 818, 831 (1st Cir. 1992) (late fees included); Fisher v. First Nat'l Bank of Omaha, *supra* note 35, at 258-61 (cash advance fees included).

[80] *Id.* (citing letter from Julie L. Williams, Chief Counsel, OCC, to John L. Douglas, Alston & Bird, LLP (Feb. 17, 1995))

Although most courts that heard *Spellman*-type cases arrived at the same conclusion as the Third Circuit, the Supreme Court of New Jersey created a conflict with *Spellman*-type decisions in *Sherman v. Citibank (South Dakota), N.A.*[81] Sherman, a resident of New Jersey, claimed that a late fee charged by Citibank, a national bank organized in South Dakota, violated New Jersey's Retail Installment Sales Act of 1960.[82] The *Sherman* case, as with *Spellman*, hinged on the interpretation of the word "interest" as used in section 85. Relying on a literal reading of *Marquette* (finding section 85 applying only to interest rates), a conflict between a 1964 and a 1986 OCC interpretation[83] of the word "interest," and the clear language of New Jersey's statute,[84] the Court concluded that interest only includes periodic finance charges and not fees.[85]

With the law in conflict over the definition of the word "interest," the Supreme Court in 1996 agreed to review the lower court's decision in *Smiley v. Citibank (South Dakota), N.A.*,[86] a section 85 case involving a South Dakota bank, a late fee, and a California usury statute.[87] Unlike lower courts, which had to sift through statutory language, legislative history, congressional purpose, and existing case law, the Supreme Court had the benefit of an official regulation issued by the OCC just two months before it heard the case.[88] The OCC's regulation interpreted

---

[81] 668 A.2d 1036 (N.J. 1995).
[82] *Id.* at 1040 (citing N.J. STAT. ANN. § 17:13A-2(g) (West 1995)).
[83] *Compare* Letter from James J. Saxon, Comptroller of the Currency (June 25, 1964) *with* OCC Interpretive Letter No. 452 from Robert B. Serino, Deputy Chief Counsel, OCC (Aug. 11, 1988).
[84] N.J. STAT. ANN. § 17:13A-2(g) (West 1995).
[85] *Sherman*, 668 A.2d at 1042-48.
[86] 900 P.2d 690 (Cal. 1995), *aff'd*, 517 U.S. 735 (1996).
[87] For a detailed explanation of *Smiley* and its impact on administrative law theory, see Robert W. Guazzo, *Smiley v. Citibank (South Dakota), N.A. – It's All About Deference to Your Elders' Chevron Difference*, 16 ANN. REV. BANKING L. 517 (1997).
[88] The OCC's interpretation was put out for comment on March 3, 1995, and adopted on February 9, 1996. *Smiley* was argued in front of the Supreme Court on April 24, 1996. The OCC interpretation is as follows:

> The term "interest" as used in 12 U.S.C. § 85 includes any payment compensating a creditor or prospective creditor for an extension of credit, making available of a line of credit, or any default or breach by a borrower of a condition upon which credit was extended. It includes, among other things, the following fees connected with credit extension or availability: numerical periodic rates, late fees, not sufficient funds (NSF) fees, overlimit fees, annual fees, cash advance fees, and membership fees. It does not ordinarily include appraisal fees, premiums and commissions attributable to insurance guaranteeing repayment of any extension of credit, finders' fees, fees for document preparation or notarization, or fees incurred to obtain credit reports.

"interest" as used in section 85 to include a wide range of fees that card issuers charged, including late fees, over limit fees, annual fees, and cash advance fees.[89] Writing for a unanimous Court, Justice Scalia analyzed the case using general principles of administrative law. Resolving the fee issue required just two inquiries: first, whether the Comptroller's interpretation was entitled to deference;[90] second, if it was, was the Comptroller's interpretation "arbitrary or capricious"?[91] Answering the first question in the affirmative, the Court reasoned that the OCC, as the implementing agency of the NBA, was empowered with the discretion to resolve any of the act's statutory ambiguities.[92] In addition, it noted that the agency followed the appropriate notice-and-comment procedures in issuing its rule.[93] The Court then determined that the Comptroller's interpretation was an acceptable one.[94] It reviewed dictionary definitions of the word "interest" and compared them with the text of section 85.[95] In the end, the Court did not find the OCC's interpretation unreasonable or in direct conflict with the NBA's language (the threshold established by prior administrative case law).[96] The Court ultimately upheld the decision of the Supreme Court of California to dismiss Smiley's usury claim for not stating a cause of action.[97]

As after the *Marquette* case, card issuers faced little NBA-related litigation in the years immediately following *Smiley*. Both cases seemed to firmly establish that states could not enforce any price-related regulations against out-of-state national banks. The decisions also strengthened OCC interpretations by setting for them a relatively deferential standard of judicial review of not

---

61 Fed. Reg. 4869 (to be codified in 12 C.F.R. § 7.4001(a)).
[89] *Id.*
[90] *Smiley*, 517 U.S. at 744-45 (citing Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 844 (1984)).
[91] *Id.* at 742 (citing Chevron U.S.A. Inc. 467 U.S. at 844).
[92] *Id.* at 739-41.
[93] *Id.* at 741.
[94] *Id.* at 744-47.
[95] *Id.*
[96] *Smiley*, 517 U.S. at 744-47.
[97] *Id.* at 747. Despite *Smiley*, nationally chartered credit card issuers continue to defend themselves, albeit infrequently, against claims that non-home-state fee regulations apply. *See, e.g.*, Kent v. Bank of Am., 2003 WL 327465 (Cal. App. 2003) (rejecting assertion that national bank organized in Arizona is subject to fee limitations imposed by California statute when bank lends money to a customer in California).

"arbitrary or capricious." Despite these developments, it seemed clear that non-home-state banking regulations outside of the scope of section 85 were still permissible.

C. Preemption Under Section 24(Seventh) of the NBA

In 2000, the California legislature passed a law that required credit card issuers to warn consumers about the dangers of making only a minimum credit card payment (generally 2 percent of the balance) each month.[98] This legislation was opposed by the credit card industry and ultimately vetoed by Governor Gray Davis.[99] The following year, Citibank and other card issuers worked with the legislature to craft what legislators termed a "compromise" disclosure bill.[100] Governor Davis signed that bill in September 2001.[101] Shortly after the bill's passage, a group of large credit card issuers, including Citibank, petitioned a U.S. District Court judge to enjoin the state from implementing the law.[102] The issuers argued that the minimum payment statute, as it applied to nationally chartered banks, was preempted by the NBA.[103] On June 28, 2002, just a few days before certain provisions of the bill were to take effect, the judge granted the issuers a preliminary injunction.[104]

---

[98] *See* Cal. A.B. 1963 (2000) (describing disclosure requirements); Michele Heller, *California Governor Vetoes Disclosure Bill For Credit Cards*, AMERICAN BANKER, Oct. 3, 2000, at 2 (describing legislative history of statute).

[99] *Id.*

[100] *The Battle Over Minimum Payments,* CREDIT CARD MANAGEMENT, July 25, 2002, at 6.

[101] The compromise bill that Davis signed required card issuers to place the following warning on the front of consumers' credit card statements: Minimum Payment Warning: Making only the minimum payment will increase the interest you pay and the time it takes to repay your balance." It also required that issuers either create a customized disclosure regarding the amount of time it would take the cardholder to pay off his or her balance if he or she made only the minimum payment required or provide a generic disclosure (e.g., "A five thousand dollar ($5,000) balance will take 40 years and two months to pay off at a total cost of sixteen thousand three hundred five dollars and thirty-four cents ($16,305.34). This information is based on an annual percentage rate of 17 percent and a minimum payment of 2 percent or ten dollars ($10), whichever is greater."). It also required that issuers provide consumers with a toll-free phone number that they could use to find ont payoff information. The disclosure associated with that provision was as follows: "For an estimate of the time it would take to repay your balance, making only minimum payments, and the total amount of those payments, call this toll-free telephone number: (Insert toll-free telephone number). CAL. CIV. CODE § 1748.13 (2003).

[102] Am. Bankers Ass'n v. Lockyer, 239 F. Supp. 2d 1000 (E.D. Cal. 2002). *See also The Battle Over Minimum Payments, supra* note 94, at 6 (describing card issuers' legal maneuvers).

[103] *Id.*

[104] *Id.*

The card issuers, represented by the American Bankers Association, sued Bill Lockyer, the Attorney General of California, challenging the constitutionality of the new law.[105] The issuers claimed that the start-up costs of the program, including printing the disclosures and staffing a special phone unit for the first six months, totaled over $20 million.[106] The issuers also asserted that the warnings were misleading and a provision regarding credit counseling information was not necessarily effective.[107] Above all, the issuers claimed that the statute was preempted by the NBA.

The issuers, however, did not solely rely on section 85 to argue that California's disclosure law should be preempted. Section 85 of the NBA, as discussed above, generally preempts non-home-state regulation of *price-related* card features (i.e., those involving "interest"). The statute at issue in *Lockyer* did not involve interest or fees; it involved disclosures. As such, the issuers primarily asserted their preemption claim under a different section of the NBA: section 24(Seventh).[108] That section, they argued, gives national banks the power to lend money without being "burdened" by costly state regulations, like those imposed by California's disclosure bill.[109]

Ultimately, the OCC filed an amicus brief in support of the national banks' position.[110] It explained that the OCC had the authority to assess the burdens that state laws placed on national

---

[105] *Am. Bankers Ass'n*, 239 F. Supp. 2d at 1000.
[106] *Id.* at 1005.
[107] *Id.* at 1006. The credit counseling information was to be provided as follows:

> In addition, the cardholder shall be provided with referrals or, in the alternative, with the "800" telephone number of the National Foundation for Credit Counseling through which the cardholder can be referred, to credit counseling services in, or closest to, the cardholder's county of residence. The credit counseling service shall be in good standing with the National Foundation for Credit Counseling or accredited by the Council on Accreditation for Children and Family Services. The creditor is required to provide, or continue to provide, the information required by this paragraph only if the cardholder has not paid more than the minimum payment for six consecutive months, after July 1, 2002.

CAL. CIV. CODE § 1748.13 (2003).
[108] 12 U.S.C. § 24(Seventh) (2004).
[109] *Lockyer*, 239 F. Supp. 2d at 1016.
[110] Brief of Amicus Curiae of The Office of the Comptroller of the Currency, *Lockyer*, 239 F. Supp. 2d 1000 (E.D. Cal. 2002).

banks.[111] Having reviewed the California law, the OCC determined that the disclosures imposed substantial direct and indirect costs on the issuers' lending activities.[112] In addition, the OCC found that the minimum payment warning intruded "massively" on the first page of consumers' credit card billing statements.[113] The additional postage, printing, paper, and processing costs, the agency reasoned, infringed on the power of national banks to lend money: a power explicitly provided for in section 24(Seventh) of the NBA.[114] Citing a number of key federal preemption cases, the OCC explained that any state or local restriction that represents an obstacle to a national bank's lending power is preempted by operation of the Supremacy Clause.[115]

The U.S. District Court for the Eastern District of California agreed with the issuers and the OCC and granted the national banks a permanent injunction.[116] Central to the case's outcome was section 24(Seventh) of the NBA and the OCC's determination that California's law was overly burdensome. Reviewing a host of NBA cases, the court found that any state law that "impair[s] the efficiency" of national banks is unenforceable.[117] Efficiency impairing laws, in the court's view, include any state regulations that increase a national bank's operating costs or hinder its marketing activities.[118] Based on the OCC's estimation that the California disclosure law would impose significant costs on national banks, the court ultimately concluded that the law represented a significant interference with the powers granted national banks by the NBA.[119] It also noted that state consumer protection laws had not traditionally been enforceable against national banks.[120]

---

[111] *Id.* at 2.
[112] *Id.* at 3.
[113] *Id.* at 20.
[114] *Id.* at 4-5.
[115] Amicus Curiae of OCC, *supra* note 104, at 14-15.
[116] *Lockyer*, 239 F. Supp. 2d at 1022.
[117] *Id.* at 1012.
[118] *Id.* at 1015.
[119] *Id.* at 1018.
[120] *Id.* at 1016 (citing Bank of Am. v. City and County of San Francisco, 309 F.3d 551, 559 (9th Cir. 2002)).

In an effort to clarify the applicability of state regulation to national banks in light of *Lockyer* (and to settle legal issues raised by other kinds of state consumer protection statutes), the OCC issued rules expounding on section 24(Seventh) in January 2004.[121] Based on previous court decisions and theories of express and conflict preemption, the OCC explained that state regulation of a national bank involving any of the following were impermissible: advertising, non-interest charges, credit account management, terms of offers of credit, mandatory statements or disclosures, and, for non-home-states, interest rates and fees.[122] The OCC also asserted that the NBA limits the scope of state regulation to the following areas when they only "incidentally affect" bank lending: contracts, torts, criminal law, rights to collect debts, acquisition and transfer of property, taxation, zoning, and any other area of law that the OCC determines to be "incidental to the...lending operations of national banks."[123]

Although the OCC's rulemaking has elicited a wide range of responses,[124] a plain reading of the agency's interpretation indicates that it broadens the OCC's preemption powers.[125] The agency essentially declared that states have little or no authority to impose any consumer-protection-oriented regulation on nationally chartered banks and that any such regulation is the province of federal law.[126] This interpretation seems the logical next step in the *Marquette-Smiley-Lockyer* progression. Although it remains untested, the courts, as seen above, have historically sided with the OCC's interpretations.[127]

---

[121] OCC State Law Preemption Rules, 12 C.F.R. §§ 7.4007 - 7.4009 (2004).
[122] *Bank Activities*, *supra* note 13, at 46,123.
[123] 12 C.F.R. § 7.4008 (2004).
[124] Critics have called the proposed rulemaking a "dagger in the heart of federalism." Jody Shenn et al., *States Strike Back*, AMERICAN BANKER, Aug. 28, 2003, at 9. Proponents see it as the OCC "enhancing the value of the franchise tremendously." Douglas Cantor, *OCC Preempts in Ga. – and Details Policy*, AMERICAN BANKER, Aug. 1, 2003, at 1.
[125] *See, e.g., San Francisco – Open for Comment*, AMERICAN BANKER, Aug. 14, 2003, at 8 (summarizing OCC's proposed rulemaking).
[126] *See Bank Activities*, *supra* note 13, at 46,122-46,123 (explaining limits of state power to regulate national banks).
[127] See *supra* notes 3, 57 and accompanying text for examples of holdings that give great deference to the OCC and its interpretations.

Overall, *Lockyer* and the OCC's recent rulemaking create a second legal theory on which card issuers can base a claim that state laws are preempted. The first theory, based on section 85, provides that non-home-state consumer protection regulations that are price-related (i.e., involving "interest") are preempted by any home-state price regulation. This is the theory on which issuers relied in *Marquette* and *Smiley*. The second theory is based on section 24(Seventh) and card issuers in *Lockyer* relied on it. It provides that when a state consumer protection regulation does not involve a credit card's price (i.e., "interest"), it is automatically preempted, regardless of whether it emanates from a home- or non-home state. The OCC's interpretation of the NBA with regard to this latter type of preemption is what triggered the current debate over the NBA. This debate, and its consequences, will be examined later in this paper.

D. Complexities of Section 85 and 24(Seventh) Preemption

As explained earlier, the division of NBA preemption into two discrete strands (i.e., section 85 and 24(Seventh)) is somewhat of a simplification. There may not always be a bright line that distinguishes price-related consumer protections from non-price-related protections. For this reason, section 85 and 24(Seventh) claims are not likely mutually exclusive.[128] Consider, for example, if a state were to pass a disclosure statute that applied exclusively to credit card loans with interest rates in excess of 28 percent. A nationally chartered credit card bank could argue that such a statute is preempted by section 85 to the extent it is price related and section 24(Seventh) to the extent it places a burden on the bank's lending operations. An argument very similar to this one was successfully made in *Lockyer*.[129] Overall, the distinction between section 85 (i.e., price-related) and 24(Seventh) (i.e., non-price-related) preemption may not always be very clear.

---

[128] *See generally* Schiltz, *supra* note 60, at 560-65 (describing expansion of section 85's scope to include lending terms beyond interest rates and fees).

[129] The banks argued that section 1748.13(f) of the California law violated section 85 of the NBA because it exempted from the disclosure statute banks that charged no interest on their loans. *Lockyer*, 239 F. Supp. 2d at 1014.

It is also somewhat of a generalization to assert that, under section 24(Seventh), all non-price-related state regulation, whether emanating from home-states or non-home states, is preempted. While this is the current position of the OCC, existing federal consumer protection legislation alludes to at least a theoretical possibility of allowing states to impose stricter regulation.[130] For example, the Truth in Lending Act expressly allows states to enact disclosure statutes as long as they are not "inconsistent" with the federal scheme.[131] Attorney General Lockyer argued unsuccessfully that this provision gave California the right to enforce its disclosure regulations.[132] Although the District Court in *Lockyer* did not find this argument persuasive,[133] it is likely that this argument will be raised in the future. It is also possible that states could indirectly regulate national banks by framing consumer protection issues as within the boundaries of state law. For example, contract law has historically been the domain of states. If a state were to declare certain provisions of the contracts between card issuers and cardholders invalid under state contract law, the state's action might have immunity from the OCC's preemptive reach. While these theories remain largely untested, they represent a few ways by which states may circumvent section 24(Seventh)'s broad reach and regulate non-price credit card terms.

---

[130] *See, e.g.*, 15 U.S.C. § 1610(a)(1) (2004) (explaining how state statutes that are not inconsistent with federal disclosure standards are not preempted).

[131] The Truth in Lending Act directly addresses how it affects state laws as follows:

> [The provisions of this act involving credit transactions and the advertising of credit] do not annul, alter, or affect the laws of any State relating to the disclosure of information in connection with credit transactions, except to the extent that those laws are inconsistent with the provisions of this title, and then only to the extent of the inconsistency.

15 U.S.C. § 1610(a)(1) (2004).

[132] *Lockyer*, 239 F. Supp. 2d at 1009.

[133] The Court concluded the following: "the express language of the savings clause indicates that its anti-preemptive effect is limited to TILA. The text provides no indication that the savings clause reaches beyond TILA to control the preemption analysis applicable under any other federal laws, including the federal banking laws." *Id.*

III. Card Industry Development as a Result of the Expanding Scope of NBA Preemption

The legal decisions discussed in the previous section significantly altered the economics and competitive landscape of the credit card industry. This section will examine how *Marquette*, *Smiley*, *Lockyer*, and OCC rulemaking affected credit card issuers and cardholding consumers.

Economists and other scholars partially credit the Supreme Court's decision in *Marquette* with triggering a rapid expansion of our nation's credit card industry and significant increases in the availability of, and access to, consumer credit.[134] The state of the economy at the time of the ruling, however, likely played an important role in shaping this outcome. Announced in December 1978,[135] the Court decided the *Marquette* case during a time of much economic turmoil.[136] Overall, the mid- to late 1970s were marked by high inflation and increasing interest rates.[137] Card issuers, who had done very well in the early part of that decade,[138] found their spreads (i.e., the difference between the rate they charged cardholders to borrow and the rate issuers had to pay for funds) shrinking.[139] In the majority of states that had adopted usury laws, the interest rates issuers needed to charge to maintain profitability began to exceed the rates allowed by state rate ceilings.[140] The Minnesota statute at issue in *Marquette*, for example, capped credit card loan interest rates at 12.0 percent.[141] According to the Federal Reserve, the federal funds rate, the rate at which banks lend money unsecured to each other overnight, was over 10.0

---

[134] *See, e.g.*, EVANS & SCHMALENSEE, *supra* note 37, at 71-72 (describing impact of *Marquette*); Ellis, *supra* note 45 (describing effect of *Marquette*); Kartik Athreya, *The Growth of Unsecured Credit: Are We Better Off?*, 87 ECONOMIC QUARTERLY 11 (Federal Reserve Bank of Richmond) (Summer 2001) (describing impact of *Marquette*); Lawrence M. Ausubel, *Credit Card Defaults, Credit Card Profits, and Bankruptcy*, 71 AM. BANKR. L.J. 249 (1997) (describing impact of *Marquette* and interest rate deregulation).

[135] *Marquette*, 439 U.S. at 299.

[136] *See, e.g.*, J. Bradford DeLong, *The Shadow of the Great Depression and the Inflation of the 1970s*, Federal Reserve Bank of San Francisco Economic Letter 98-14 (May 1, 1998), *at* http://www.sf.frb.org/econrsrch/wklyltr/wklyltr98/el98-14.html (describing some of the economic problems policymakers faced in 1970s, including inflation and the oil embargo).

[137] EVANS & SCHMALENSEE, *supra* note 43, at 71.

[138] Card issuers did well because prevailing interest rates were low. This allowed them to borrow money at a low rate and lend it out at a higher rate.

[139] *Id.*

[140] Ellis, *supra* note 45.

[141] *Marquette*, 439 U.S. at 302.

percent in 1978 and reached as high as 19.1 percent in June 1981.[142] Considering that banks also incur expenses associated with operations, marketing, and chargeoffs, credit card lending in the late 1970s and early 1980s would not have been feasible in states with low rate ceilings. As a result, issuers stopped marketing cards to consumers in states with interest rate ceilings that were at or below the costs required to fund the loans.[143]

Immediately after the Supreme Court allowed issuers to export home-state interest rates with its *Marquette* decision, various state legislatures scrambled to entice nationally chartered credit card issuers to relocate to their states by repealing or amending their usury statutes.[144] South Dakota, for example, attracted Citibank's credit card operations away from New York by raising its state interest rate ceiling to 19.8 percent.[145] Similarly, MBNA and three other large, Maryland-based card lenders moved their operations to Delaware after that state repealed its rate ceiling and made creditor-friendly amendments to its consumer lending laws.[146] Ultimately, between 1980 and 1985, a total of 15 states did away with their rate ceilings, and many raised rate ceilings to accommodate creditors.[147]

As states liberalized lending statutes and card issuers took advantage of interest rate exportation, the card industry and, in particular, nationally chartered card issuers, flourished (see Figure 1). The Federal Reserve reported that total U.S. revolving credit grew 172 percent between 1978, the time of the *Marquette* decision, and 1985.[148] The percentage of U.S. families that held

---

[142] Federal Reserve Statistical Release H.19 (available at http://www.federalreserve.gov/releases/h15/data.htm).
[143] LEWIS MANDELL, THE CREDIT CARD INDUSTRY 100 (1990).
[144] *See, e.g.*, EVANS & SCHMALENSEE, *supra* note 44, at 72 (explaining how state legislatures modified usury laws to attract card issuers); Ellis, *supra* note 45 (same).
[145] Glenn B. Canner & Charles A. Luckett, *Developments in the Pricing of Credit Card Services*, FEDERAL RESERVE BULLETIN (September 1992) at 654.
[146] Ellis, *supra* note 45, at n.15. It is interesting to note that in 1981, national banks located in Delaware had a total of $8,000 in outstanding on-balance-sheet credit card loans, or 0.003 percent of the U.S. total. Five years later, nationally chartered Delaware banks held over $10 billion in on-balance-sheet credit card loans, or 16 percent of the national total. OCC Quarterly Journal, 1Q1982 and 1Q1987.
[147] Canner & Luckett, *supra* note 145, at 654.
[148] From December 1978 to December 1985, revolving credit grew from $48.3 billion to $131.6 billion. Federal Reserve Statistical Release G.19 (Consumer Credit) (*available at* http://www.federalreserve.gov/releases/g19/hist/cc_hist_r.txt). Revolving credit includes unsecured

bank-type credit cards (e.g., MasterCard, Visa) increased from 38 percent in 1977 to 55 percent in 1986.[149] From 1983 to 1986, the portion of consumer debt payments that went to credit card issuers increased 50 percent, and the average credit card balance of consumers who carried a balance increased from $969 to $1,472.[150] The expansion of credit during this period particularly affected lower income consumers.[151] The percentage of households earning less than $10,000 who held a credit card increased from 28 percent in 1977 to 42 percent in 1986.[152] Overall, *Marquette*, and an economic expansion that started in the early 1980s, helped trigger a period of unprecedented credit card purchasing and borrowing.[153]

Despite its age, the *Marquette* interpretation of the NBA continues to strongly influence the structure and organization of the credit card industry. Consider Delaware, South Dakota, Nevada, Arizona, Rhode Island, and New Hampshire – six states that are home to 4 percent of the country's population. As of September 2003, the national banks located in these states were owed over $350 billion of the $490 billion in U.S. consumer credit card loans.[154] This concentration of very large credit card banks in only a few states is a direct result of the NBA's allowing the creditor-friendly laws of these states to be exported throughout the country.

---

obligations such as credit card loans and consumer installment loans. It excludes mortgages and automobile loans.

[149] Glenn B. Canner, *Changes in Consumer Holding and Use of Credit Cards, 1970-86*, 10 J. RETAIL BANKING 13, 14 (Spring 1988). Canner's study is largely based on consumer credit surveys conducted by the Federal Reserve Board.

[150] *Id.* at 20.

[151] Ellis, *supra* note 45.

[152] Canner, *supra* note 149, at 14.

[153] *Id.* at 13. Despite significant increases in the use of credit card credit, the costs of credit remained high throughout most of the 1980s. Regardless of their credit risk, consumers paid interest rates in the 18 to 19 percent range. It was not until the early 1990s that issuers began to compete on price and card interest rates fell. *See* Mark J. Furletti, *Credit Card Pricing Developments and Their Disclosure*, Federal Reserve Bank of Philadelphia Discussion Paper, at 6 (Jan. 2003) (available at http://www.phil.frb.org/pcc/discussion/discussion0103.pdf) (describing credit card pricing in the 1980s and 1990s); *The Profitability of Credit Card Operations of Depository Institutions*, Report to Congress by the Board of Governors of the Federal Reserve System, August 1997 [hereinafter *Profitability Report*] (*available at* http://www.federalreserve.gov/boarddocs/rptcongress/creditcard/1997/default.HTM#N_13_) (describing high APRs in 1980s). Instead of arguing that *Marquette* triggered the expansion of credit, one could argue that the emergence of consumer lending on a national scale triggered *Marquette*. Both seem plausible.

[154] Call Report Data, National Information Center, Sept. 2003 (data on file with author). These loan totals include both on- and off-balance-sheet credit card loans.